Green Investment Partners

Impact Philosophy

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Green Investment Partners – Impact Philosophy

As a sustainable investment manager with the dual focus of capital appreciation and the reduction of greenhouse gas emissions, impact investing is central to our philosophy and firm.

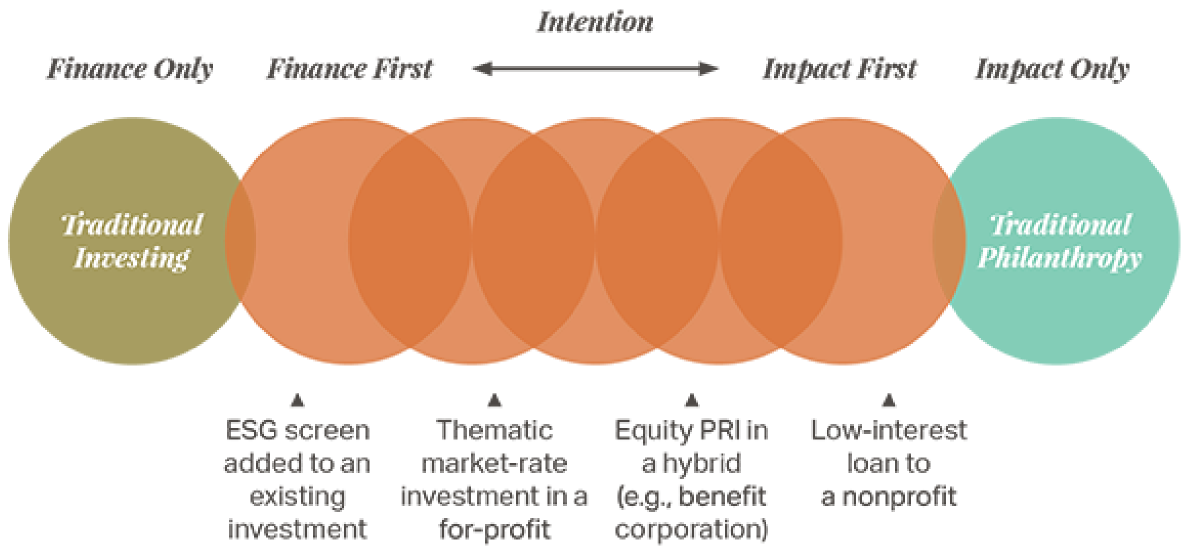
We discuss what impact investing is and how it has traditionally been viewed within the context of listed equities investing. Although difficult to measure, the scale and wider system effects of listed equities make them instrumental in achieving global impact goals and may be considered a vital impact investing mechanism.

Green Investment Partners' intentions are to positively contribute at scale through company and system-wide impacts. We will be honest, transparent, and accountable in how we operate.

Introduction

Impact investing is defined as the intention to generate a measurable, beneficial, social or environmental impact alongside a financial return.[1] The history of socially responsible investing stretches back to early religious texts and various groups but only gained momentum throughout the latter half of the 21st century, with the phrase 'impact investing' being coined as recently as 2006.[2]

Figure 1: Impact Investing – A Balance of Commerce and Compassion[3]



Impact can be broadly split into two levels. 'Company Impact' is delivered by the underlying company's product or services, and 'Investor Impact' which refers to the change to the company from the investment activity of the investor, such as a lower cost in capital. Impact can be either positive or negative (or more realistically, some combination of both).

[1] https://thegiin.org/impact-investing/need-to-know/
[2] https://www.rockpa.org/wp-content/uploads/2020/10/RPA-Impact-Investing-Handbook-1.pdf
[3] https://www.rockpa.org/guide/impact-investing-introduction/

Traditionalist

The traditionalist view of impact investing has focused on the need for the investor's capital to provide a measurable, discrete, and additional positive impact. Therefore, under this view, any impact would not have occurred was it not for that specific investor's additional capital. This view largely excludes listed equities, as it deems owning shares as statistically irrelevant, like a single vote in a democratic election.

System-Wide

A system-wide view does not disregard the traditionalist view, but it does consider investments as part of the wider world economy and the different mechanisms which can lead to positive change. A system-wide view also considers that as the number of aligned voters in a system increases, their influence increases as well. This has clearly begun to happen within the impact investing space.

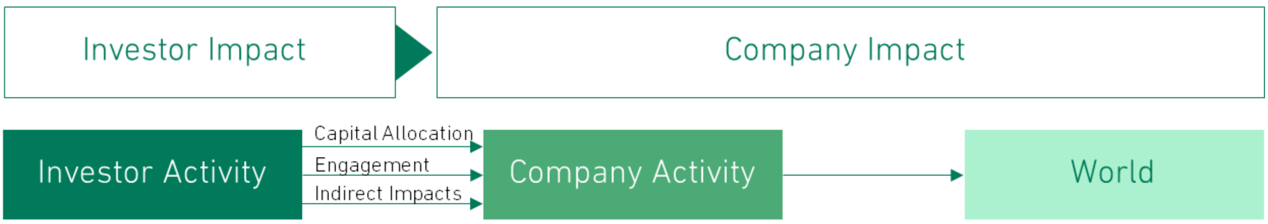
Companies, investors, and politics can and do influence each other. This interaction between different stakeholders is a reflexive relationship, and although hard to measure, its effects are significant and far-reaching.

'There is no other way to cope with the scale and severity of social and environmental issues other than to attract investment capital from the $200 trillion of investable assets in our financial system'. Ronald Cohen[4]

Traditionalist

The traditionalist view shows an investor's impact can been split into capital allocation, shareholder engagement, and indirect impacts. Traditionally, the investor impacted the company which in turn impacted the world. In reality, this relationship is reflexive and complex.

Figure 2: Traditional Impact View[5]



Capital Allocation

The traditionalist view focuses on the impact of an investor's incremental capital to a project or company. This view largely restricts impact investing to philanthropic activity or to situations where new capital is invested into illiquid markets, both listed and private.

In the private illiquid markets, the number of shareholders are fewer and the voting power per participant is generally greater. This voting power concentration is often seen as a proxy for greater impact.

Another argument for increased impact is that without a specific investor, the company or project wouldn't exist. In reality, private equity or venture capital deals are competitive, and another

[4] Impact, Reshaping Capitalism to Drive Real Change, Sir Ronald Cohen, Ebury Press, 2020
[5] The Investor's Guide to Impact, Florian Heeb & Julian Kölbel, Center For Sustainable Finance and Private Wealth, UZH, 2020

participant could invest with slightly different terms. Just because an investor can be replaced by another participant, as can happen in both liquid and illiquid markets, is not a strong argument for that investor's impact being negligible.

Other complexities should be considered, such as, is a take private deal more impactful than an initial public offering (IPO)? Are higher transaction fees of private deals always factored in?

Engagement

Listed equity investors can impact companies by directly engaging with them, which is central to the definition of impact investing by the International Finance Corporation (IFC). This can be through dialogue with a company and in conjunction with other investors on topics such as climate change, emissions reporting, diversity, corporate governance, and management incentives.

At Green Investment Partners our aim is to directly engage with companies and other investors to increase our impact. This can be in the form of shareholder voting or raising topics at shareholder meetings, in addition to direct conversations with the management.

Causal links that attributes specific impact outcomes to engagement are difficult to quantify and document. However, engagement strategies underpinned by documented activities and outcomes can strengthen claims.

Indirect Impacts

Indirect impact actions, such as signalling and excluding companies, are harder to measure but nevertheless contribute to improving the system.

Managers and investors can be public about excluding companies and their reasons for it. We are transparent about our criteria and will continue to sell companies when they move against our green criteria or do significant harm. Communication of decisions may awaken other participants to a particular issue and may persuade a company's management to act positively.

Signalling can be defined as system-wide contributions, including engagement with regulators, clients, and advisors. We want to advocate for new standards for sustainable finance, bilaterally and collectively. Communication of our research and decisions can help further inform investors on impact investing.

System-Wide

A system-wide view of impact investing considers other factors, in addition to the traditionalist view, such as size of market, reflexivity, politics, behavioural biases, and the cost of capital.

Voting Power

The listed equity market is over ten times[6] the size of the private market[7], and with its vast capital and voting power brings the potential for significant impact. Fast progress on climate change requires the scale that only the listed equity market can bring.

[6] https://www.sifma.org/resources/research/fact-book/
[7] https://www.ft.com/content/4d0e6f18-2d56-4175-98c5-e13559bdbc25

'If these listed equity strategies can be harnessed to intentionally drive positive impacts through their investments, then they can potentially deliver a substantial boost to progress on the SDGs' Global Impact Investing Network (GIIN)[8]

Reflexivity

In economics, the theory of reflexivity was developed by George Soros[9] and posits that ideas and events influence each other in reflexive feedback loops, leading to procyclical virtuous or vicious cycles. Put into context, the theory encompasses the idea that investors don't base their decisions on reality, but rather on their perceptions of reality instead. This, in turn, impacts fundamentals, perceptions and prices. During the global financial crisis, rising house prices induced banks to increase mortgage lending and this in turn raised prices further and resulted in a price bubble.

Traditionalist views of impact investing do not factor in reflexivity as an impact mechanism. For example, the traditionalist view is that regulators influence companies, however companies can also influence the regulator. For example, companies lobbying government can lead to favourable regulations, which in turn strengthens their position, and increases their power and lobbying efforts. It is hard to measure, but reflexivity should not be disregarded or underestimated.

With the increasing popularity of environmental, social and governance (ESG) investing and organisations such as the Principles for Responsible Investment (PRI) covering $121 trillion in AUM[10], the virtuous reflexive cycle towards responsible investing is undeniable. This is already having a real-world impact on the underlying companies and governments, with better technologies, reporting, net zero strategies and policies.

Figure 3: System-Wide Impact View[11]

Politics Matter

In politics, the average voter's perspective on climate change is shifting. This in turn influences policy, regulations, companies, and their returns. These long-term tailwinds for companies contributing to the future economy are becoming more focused on preventing climate change. And remember, politics is also influenced by the market.

[8] https://thegiin.org/assets/Impact%20Investing%20in%20Listed%20Equities_FINAL.pdf
[9] https://www.ft.com/content/0ca06172-bfe9-11de-aed2-00144feab49a
[10] https://www.unpri.org/annual-report-2021/how-we-work/building-our-effectiveness/enhance-our-global-footprint
[11] Green Investment Partners

Company shareholder views are also changing; in the US, average support for environmental votes have gone from 36% in 2020 to 55% in 2021.[12]

Behavioural Biases

Behavioural biases, such as confirmation bias which leads to herd behaviour, remain deeply embedded in society. People care about their communities and as the evidence and immediacy of climate change piles up, more people are starting to take note. Events like COP26, the reporting of climate change-induced disasters and support for cleantech companies can help shift societies' views.

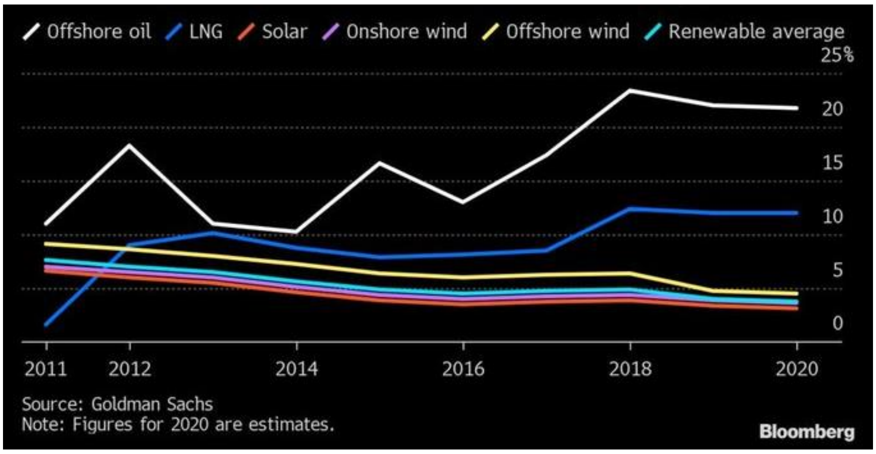
Extreme views can also have a greater impact on a system because it pushes others around them to adjust, even though they do not share these views (e.g. populism), as explained by Nassim Nicholas Taleb[13].

Cost of Capital

Cost of capital is now having a significant impact on companies. Tesla's popularity amongst investors allowed it to use the listed equity markets to access cheap capital, which had a material impact on its competitive position and enabled its growth. This in turn accelerated electric vehicle development across the industry and amongst its competitors. Tesla also received state subsidies along the way.

Contrast this with the oil and gas sector, where investors require higher returns on capital for the risk they are taking. This group of shareholders are aware of the tail risk, and they want to get paid for it. Higher costs of capital have a direct effect on the profitability of the business.

Figure 4: Cost of Capital: Fossil Fuels vs Renewable Energy[14]



[12] https://my.slaughterandmay.com/insights/client-publications/shareholder-climate-change-activism-in-the-2021-agm-season-and-whats-coming-next
[13] Nassim Nicholas Taleb, Antifragile: Things that Gain from Disorder. 2013
[14] Bloomberg, Goldman Sachs

Conclusion

The impact discussion is evolving and increasing in importance. We have less than eight years left to limit global warming to 1.5°C and prevent the worst effects of climate change.[15] Each positive impact we can make today, matters. Stating climate change will lead to sea levels rising, biodiversity loss and more extreme weather fails to grasp the uncertainty and the risk that once we hit a certain point there is no going back. The reality of complex systems is messy and often nonlinear, with the potential for unpredictable chain reactions. The environment needs to be protected and can no longer be priced as a free and limitless resource. There may become a point where the damage is near-impossible to reverse, especially with biodiversity.

Positive impact investing can occur in both private and public equity markets, with the past few years having shown this. Multiple stakeholders: across governments, companies, managers, and owners, are making progress on climate conscious investing. This is bleeding into impact investing at an ever-increasing pace, but there remains a long road ahead towards net zero.

At Green Investment Partners we will adhere to our green investment criteria, be transparent on emissions calculations and do no significant harm on other social or environmental factors. We will engage with companies, regulators, clients, and our community. We want to show that achieving a net zero economy is possible while compounding capital. We must act now for a chance to reduce the very worst effects of climate change.

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[15] https://climateclock.world/

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